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Pain in Spain May Linger as Banks Seek to Avoid Property Losses

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By Charles Penty and Sharon Smyth

Oct. 2 (Bloomberg) -- Maria Jose Lozano, a civil servant from Madrid, left a recent property fair empty-handed after discovering that home prices were still out of reach in a market where sales have dropped 50 percent from their 2006 peak.

"We came here expecting to find a bargain, or at the very least some reduced-price homes, but we've seen nothing," said Lozano, 49, after browsing through the offerings, including properties that lenders such as Banco Santander SA and Caja Madrid acquired in exchange for canceling developers' debts.

Banks bought about 110,000 homes to keep losses off their books as Spain's property bubble burst, according to real estate researcher RR de Acuna & Asociados in Madrid. Now they're using strategies reminiscent of the boom times -- 100 percent mortgages, low interest rates and free cars -- to sell homes, potentially slowing a drop in prices that's needed to spur recovery from Spain's worst recession in 60 years.

"Maybe you can create some accounting value with all these tricks, but in the end it doesn't make the situation any better and in the long term makes it worse," said Luis Garicano, a professor of economics and strategy at the London School of Economics, in a phone interview.

Spanish lenders acquired at least 20 billion euros ($29 billion) of real estate in the past 18 months, according to data compiled by analysts at Zurich-based Credit Suisse Group AG. There are as many as 1.6 million empty homes in Spain, an overhang that may take seven years to clear with annual demand running at about 218,500 units, Acuna & Asociados estimates.

Financing Terms

Instead of cutting prices, banks are offering more generous financing terms for their own properties than those being sold by third parties, said Fernando Rodriguez de Acuna, president of Acuna & Asociados.

"The banks are reducing financing costs to get rid of their housing stock, but this solution has its limits," he said in an interview. "The only way banks will be able to sell homes they haven't sold in the mid-term will be to do so at a loss."

Santander, Spain's biggest lender, has acquired more than 4 billion euros of real estate and is selling homes through Altamira Santander Real Estate, its property arm.

Altamira offers clients variable-rate mortgages at the one- year euro interbank offered rate plus 0.4 percent, according to its Web site. That's 1.64 percent at current rates. Santander offers a variable rate mortgage at Euribor plus 1 percent, according to data published by El Pais newspaper.

The bank also offers 100 percent financing, mortgage insurance and aid to buyers of holiday homes, according to the Web site. Altamira said in August that it had sold at least 1,100 of the 2,550 newly built properties it had on sale.

No Timetable

A spokeswoman for Madrid-based Santander declined to comment on whether the bank's policies were slowing a recovery. The spokeswoman, who asked not to be identified because of company policy, said Santander's booth at the property fair was informational, and it didn't try to sell homes at the event because it believes prices have adjusted to the market.

Banco Popular Espanol SA, Spain's third-biggest commercial bank, bought 2.3 billion euros of property and is selling homes through its Aliseda Gestion Inmobiliaria unit. La Caixa, Spain's biggest savings bank, throws in a free car for anyone under 35 who buys an apartment through its property company.

Banco Popular has no intention of selling homes for less than the bank thinks they're worth because low interest rates mean the cost of holding them is comparatively cheap, Chief Financial Officer Jacobo Gonzalez-Robatto said in July.

"We don't have any timetable," he said at the bank's earnings press conference.

Lagging Behind Ireland

The tactics employed by banks mean house prices are adjusting more slowly in Spain than other countries, said the LSE's Garicano.

Spanish home prices have declined 8.3 percent from their peak in the fourth quarter of 2007, according to the National Statistics Institute. That compares with a 25 percent drop in Ireland, a report by Irish Life & Permanent Plc shows. The decline is 12 percent in the U.K., according to Hometrack Ltd.

By other measures, Spain has been harder hit by the global recession than other European countries.

Eurostat data show that Spain has the highest unemployment rate in Europe at 18.5 percent, and the Organization for Economic Cooperation and Development forecasts the economy will continue to shrink next year as other European nations start to recover. The Spanish economy may contract 0.9 percent next year, making it the worst performer in the 30-nation OECD after Hungary and Ireland, the Paris-based group forecast in June.

Orderly Decline

Carlos Solchaga, Spain's finance minister from 1985 to 1993, said banks have succeeded in putting a break on price declines and preventing the fire sale seen in other countries.

"The banks are doing what they have to do," said Solchaga, who now heads Solchaga Recio & Asociados, a Madrid- based consulting firm. "The reality is that they are contributing to the process of price reductions."

Caixa Catalunya, a Barcelona-based savings bank, slashed prices on some homes as it sold 600 of the 3,700 properties it had on offer. About half of the homes sold for 30 percent less than the offer price and a quarter brought discounts of 10 percent to 20 percent, said Pol Clota, the bank's commercial director for real estate. The rest were sold for full price.

"If we have this real estate, we have to do something with it and the competition is very fierce," Clota said in an interview at the property fair.

'Unfair' Competition

Developers say they now have to compete with banks, as well as each other, to shift stocks of unsold property.

"Sometimes that competition is unfair in that they can offer better financing," said Ignacio Iglesias, a spokesman for Nozar SA, a closely held developer that filed for protection from creditors in September.

Spanish banks acquired homes from developers to cushion the impact of a property crash that increased loan-loss provisions by 70 percent to 9.7 billion euros in the first half, according to central bank data. Bad loans as a proportion of lending rose to a 13-year high of 4.73 percent in July and may exceed 8 percent over the next year, Credit Suisse estimated last month.

The problem is that banks may have taken real estate onto their books using valuations that don't describe their true value, said the LSE's Garicano. In a market where transactions have collapsed and some appraisals are based on sellers' asking prices, valuations may bear little relation to what buyers are prepared to pay, he said.

While the Bank of Spain requires lenders to set aside a provision equal to 10 percent of a property's balance sheet value, they may be forced to report additional losses if asset values drop below the amount of the original debt.

'Significant Losses'

"Some banks won't let prices fall because they don't want to recognize their losses," said Pedro de Churruca, general director for Spain of property broker Jones Lang LaSalle in Madrid. "Significant losses would emerge if they did that."

Back at the property fair, Lozano and her husband, Fernando Cano, watched as lines of would-be buyers formed alongside the stands run by Caja Madrid and Pryconsa, a developer that now has to compete with banks to sell its properties.

About 40,000 people attended the three-day fair, according to IFEMA, the organizer of the event. Three more are planned during the next year.

"Prices haven't dropped and buyers won't return to the market until they do," Cano said.

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